[JOINT COMMITTEE PRINT]

COMPARATIVE DESCRIPTION

OF

H.R. 6300

(THE TAX COMPLIANCE ACT OF 1982)

AND

H.R. 5829

(THE TAXPAYER COMPLIANCE IMPROVEMENT ACT OF 1982)

SCHEDULED FOR A HEARING BEFORE THE COMMITTEE ON WAYS AND MEANS ON MAY 18, 1982

PREPARED BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

The Committee on Ways and Means has scheduled a hearing on May 18, 1982, on the bills, H.R. 5829 (Mr. Conable) and H.R. 6300 (Mr. Rostenkowski) which relate to improving compliance with the Federal income tax laws. H.R. 5829 is identical to S. 2198, on which the Subcommittee on Oversight of the Senate Committee on Finance held a hearing on March 22, 1982. (A description of S. 2198 is in a prior Joint Committee staff pamphlet, JCS–6–82.)

This pamphlet, prepared in connection with the May 18, 1982 hearing, contains a comparative description of the provisions of H.R. 5829 and H.R. 6300. The comparative description is preceded by an overview of the bills.

OVERVIEW

H.R. 6300 (The Tax Compliance Act of 1982)

H.R. 6300 (introduced by Chairman Rostenkowski) is intended to improve compliance with the income tax laws by adopting a number of new provisions which adddress six specific tax compliance challenges. First, the bill would discourage willful disregard for the income tax system by criminals, promoters of abusive tax shelters, fraudulent tax advisors and tax protestors. Specifically, there would be new provisions allowing the Internal Revenue Service to use jeopardy and termination assessment procedures to tax cash connected with illegal activities. Significant restrictions would be placed on the issuance of bearer debt obligations to the public, thus restricting one medium of exchange in the illegal sector and reducing the ability of persons to avoid tax with respect to such activities. New civil penalties would be imposed on promoters of abusive tax shelters, persons assisting in the presentation of false tax documents, and persons filing tax protest returns. In addition, taxpayers would be required to assume a greater burden to block third-party recordkeeper summonses.

Second, the information reporting system would be significantly expanded and strengthened. Reporting would be required on accruals of interest and original issue discount transactions on certain bearer instruments, on independent contractors and direct sellers, on transactions through certain brokers, including barter exchanges, on State and local tax refunds, and on casualty insurance reimbursements. The penalties for failure to comply with information reporting requirements would be increased and a withholding tax would be imposed on persons who fail to supply their taxpayer identification numbers or supply incorrect numbers.

Third, compliance with respect to pension and annuity payments would be strengthened through improved recordkeeping and reporting and imposition of withholding in the absence of an election by the taxpayer not to have withholding apply.

Fourth, reporting, examination and litigation with respect to tax liability on foreign activities would be streamlined through provisions designed to permit simplification of returns and information statements on such activities, to strengthen the penalties for failure to file required returns and statements, and to assure access to records maintained outside the United States.

Fifth, the rules relating to computation of interest on both underpayments and overpayments of tax would be amended to require compounding, to limit interest payments when taxpayers fail to file returns or claims for refunds or adjustments promptly, and to increase the cost of substantial underpayments.

Finally, the bill would simplify the administrative examination of income tax issues arising with respect to partnerships and subchapter S corporations by providing for a single administrative proceeding with respect to such issues. The bill would also provide for review of the administrative determination in a single judicial proceeding.

H.R. 5829 (The Taxpayer Compliance Improvement Act of 1982)

H.R. 5829 (introduced by Mr. Conable) is intended to reduce taxpayer noncompliance through a series of provisions designed to encourage complete and accurate reporting of income and deductions. The bill includes provisions improving information reporting, increasing penalties for noncompliance, amending the methods under which interest is computed and substantially revising the withholding rules for pension distributions. Under the bill interest on bearer obligations and obligations of the United States, charged tips, transactions involving securities and commodities, and State and local income tax refunds would be subjected to new reporting requirements. The bill's penalty provisions include a minimum penalty for extended failure to file returns; a substantial increase in the penalty for failure to supply taxpayer identification numbers or to file information returns, and withholding in cases of continuing violations; a 10-percent penalty for any substantial underpayment of tax when the items giving rise to the underpayment were not disclosed on the return; and a penalty on corporate officers and agents, including attorneys and certified public accountants, who commit fraud with respect to a corporation's tax. The interest proposals include provisions for adjusting the interest rate payable by or to the Treasury, and compounding such interest, semiannually. Where applicable, these provisions would cover foreign as well as U.S. transactions.

COMPARATIVE DESCRIPTION OF H.R. 6300 AND H.R. 5829

I. CRIMES, ABUSIVE TAX SHELTERS, FRAUD, ETC.

A. Treatment of Items Used in Illegal Activities

1. Special rules with respect to certain cash (sec. 101 of H.R. 6300)

Present law

In the usual case, the Secretary may not assess and collect a tax deficiency unless he follows certain procedures designed to allow the taxpayer to first contest the existence and amount of the deficiency. These procedures include written notice of deficiency followed by a 90-day period during which time the taxpayer may petition the Tax Court for review of the Secretary's determination. No assessment may be made until after this 90-day period has expired or until after a decision of the Tax Court is final. Jeopardy and termination assessment procedures are provided when the Secretary believes the collection of a tax will be jeopardized by delay. These procedures permit immediate assessment and collection of the tax; that is, the taxpayer is denied the opportunity to contest the liability prior to payment.

Jeopardy assessment

If the Secretary believes that the assessment and collection of a deficiency of income, estate, gift or certain excise taxes will be jeopardized by delay, he may assess such deficiency and demand its immediate payment. Examples of cases in which the Secretary may reasonably believe that collection of a tax is in jeopardy include cases in which the taxpayer intends to conceal himself or his property from the Secretary, remove his property from the United States, or dissipate his property. If after assessment, notice, and demand the taxpayer fails to pay the assessed amount, the Secretary may immediately enforce collection.

The taxpayer is entitled to an expedited review by the Internal Revenue Service of the determination of jeopardy and the reasonableness of the amount assessed. After review by the Internal Revenue Service, the taxpayer is also entitled to a review by the appropriate United States District Court. In the District Court, the Secretary has the burden of proving that the determination of jeopardy was reasonable under the circumstances, while the taxpayer has the burden of proof with respect to the amount assessed. This review procedure is directed only at the reasonableness of the jeopardy assessment and the amount assessed. The District Court's opinion is nonappealable, and is not a determination of the actual existence or amount of any deficiency due from the taxpayer.

The taxpayer is also entitled to a separate review by the District Court or Tax Court of the actual existence of any tax deficiency on which the jeopardy assessment was based.

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Termination assessment

When the Secretary finds that the collection of an income tax with respect to the current or immediately preceding taxable year (before the due date of the return for the preceding taxable year, with extensions) is in jeopardy, he may immediately terminate the taxable year, and assess and demand any deficiency he reasonably believes owing with respect to the tax period ending on the date of assessment. The taxpayer is entitled to the same administrative and District Court review of the termination assessment as is the case with jeopardy assessments. The taxpayer is also entitled to normal District Court or Tax Court review of the Secretary's determination that a deficiency for that taxpayer existed. To facilitate this review, the Commissioner must mail a notice of deficiency to the taxpayer within 60 days of the later of the due date of the taxpayer's return for the taxable year of the termination assessment, or the date the taxpayer files such return.

Both the jeopardy and termination assessment procedures require the Secretary to determine that there is a deficiency in tax and that the collection of this deficiency is in jeopardy. These procedures are not, therefore, well suited to cases in which the Secretary has reason to believe that a tax is owing with respect to an amount of property (for example, cash), but cannot determine the proper owner of such property.

H.R. 6300

H.R. 6300 would define two cases in which the Secretary could presume that the collection of an amount of income tax is in jeopardy. First, if a person possesses, controls, or deposits, or has recently possessed, controlled, or deposited cash or its equivalent, and the Secretary believes that such cash represents gross receipts from, or funds used in, an illegal activity, then the Secretary will be able to presume for purposes of the jeopardy or termination assessment provisions (1) that the entire amount of the cash is gross income, and (2) that the collection of the tax owing with respect to such gross income is in jeopardy.

Second, if an individual in physical possession of more than $10,000 of cash or its equivalent denies ownership of the cash and cannot reasonably identify the true owner, then the Secretary will be permitted to presume, for purposes of the jeopardy and termination assessment provisions (1) that the collection of tax on such cash is in jeopardy, and (2) that the cash is taxable to a single individual at the 50-percent rate. The Internal Revenue Service could not assess on the same cash twice. Notices with respect to the assessment and the right to contest the assesment would be given to the person found in possession of the cash; however, the true owner could come forward and challenge the assessment and would be retroactively substituted for the possessor for all purposes as of the date of the original assessment. In addition, the true owner would continue to have the same rights as exist under present law to recover his cash.

H.R. 6300 would also provide that, for purposes of any law requiring reporting of monetary instruments in excess of $5,000, transported between the United States and a point outside the United States, an attempt to transport shall be subject to the same reporting requirements as apply to the act of transporting.

These amendments would be effective on the day after enactment.

H.R. 5829

No provision.

2. Obligations required to be registered (sec. 102 of H.R. 6300)

Present law

Under present law, the tax status of debt obligations is generally the same regardless of whether the obligation is issued in registered form or in bearer form. However, in the case of certain State and local obligations relating to housing or energy programs, interest on the obligations is exempt from Federal income tax only if the obligation is issued in registered form. Unregistered (bearer) obligations are often used in commercial dealings as effective substitutes for cash. Such obligations may, therefore, be used to conceal untaxed income.

H.R. 6300

H.R. 6300 would discourage the issuance of bearer instruments to the general public by denying certain tax benefits for such obligations and by prohibiting the issuance of bearer obligations by the Federal government. Specifically, the Second Liberty Bond Act would be amended to require that every obligation of the United States or any agency or instrumentality thereof must be in registered form. In addition, interest on an obligation of a State or local government would not be exempt from Federal income tax unless the obligation were issued in registered form. In the case of obligations issued by other than governmental units, registration would be required on all obligations except (1) obligations issued by a natural person, (2) obligations not of a type offered to the public, and (3) obligations with a maturity at issue of less than one year. Thus, most commercial paper would be exempt from the registration requirements. The Secretary would be given authority to require registration of short-term and non-public obligations if, with respect to specific types of obligations, he determines that such obligations are used frequently to evade Federal taxes.

In the case of obligations issued by other persons such as corporations, trusts, and partnerships, the issuing entity would not be permitted a deduction for interest paid on any obligation required to be registered which is not in registered form and the holder would not be permitted any loss deduction with respect to such unregistered obligations. For purposes of these new rules, an obligation would be considered issued in registered form if the right to principal and interest were determined by entries on the books of the issuer.

These new registration requirements would apply to obligations issued after December 31, 1982.

H.R. 5829

No provision.

B. Abusive Tax Shelters

1. Penalty for promoting abusive tax shelters, etc. (sec. 111 of H.R. 6300)

Present law

Present law contains no penalty provision specifically directed at promoters of abusive tax shelters and other abusive tax avoidance schemes. When a promoter sells a tax shelter that is premised on mis-

representations of the tax law, the existence of the investment assets, or the value of property or services, the promoter is not subject to any civil tax penalty unless some action of the promoter is connected with the preparation or presentation of a false or fraudulent return or other document. In such a case, the promoter may incur a civil penalty if his actions constituted return preparation. An injunction against further violation of the return preparer rules could also be sought. If the promoter is not a return preparer, then the only remedy available to the Government is criminal prosecution for aiding, assisting in, procuring, counseling or advising the preparation or presentation of a false or fraudulent return or other document under the internal revenue laws.

H.R. 6300

H.R. 6300 would impose a new civil penalty on persons who organize or participate in the sale of abusive tax shelters. An abusive tax shelter would be any partnership or other entity, any investment plan or arrangement, or any other plan or arrangement having a purported effect on Federal tax liability in connection with which the person makes or furnishes either (1) a false or fraudulent statement with respect to the allowability of any tax benefit or (2) a gross valuation overstatement (whether or not the accuracy of the statement is disclaimed). A gross valuation overstatement would be a statement of the value of services or property which exceeds 200 percent of the correct value and which is directly related to the amount of any deduction or credit allowable to any shelter participant. The penalty for promoting an abusive tax shelter would be the greater of $1,000 or 10 percent of the gross income derived or to be derived from the activity. If the Internal Revenue Service cannot determine the entire amount of the gross income from an activity, it may assess the penalty on the portion of such gross income that may be determined. The Secretary would be given authority to waive all or part of any penalty resulting from a gross valuation overstatement, when there was a reasonable basis for the valuation and the valuation was made in good faith. The mere existence of an appraisal would not be sufficient, by itself, to show either reasonable basis or good faith. As in the case with the civil fraud penalties, the burden of proof in imposing the penalty would be on the Secretary. This penalty would be in addition to all other penalties provided for by law and would apply beginning on the day after the date of enactment.

H.R. 5829

No provision.

2. Action to enjoin promoters of abusive tax shelters, etc. (sec. 112 of H.R. 6300)

Present law

Present law provides that a civil action may be brought by the United States to enjoin any person who is an income tax return preparer from (1) engaging in any conduct subject to penalty under the income tax return preparer provisions or under the criminal tax laws, (2) misrepresenting his qualifications, (3) guaranteeing a refund or credit, or (4) engaging in any other fraudulent or deceptive conduct that substantially interferes with the proper administration of the tax laws. Injunctive relief may be granted by the appropriate

United States District Court if the court finds that such relief is appropriate to prevent recurrence of the prohibited conduct.

H.R. 6300

H.R. 6300 would permit the United States to seek injunctive relief against any person who has engaged in conduct subject to the penalty for the organization or sale of abusive tax shelters (sec. 111 of H.R. 6300). These actions would be brought in the District Court of the United States for the district in which the promoter resides or has his principal place of business. If a citizen or resident of the United States does not reside in or have a principal place of business in any U.S. judicial district, such citizen or resident would be treated as a resident of the District of Columbia. The amendment would take effect on the day after the date of enactment.

H.R. 5829

No provision.

3. Procedural rules applicable to penalties under sections 6700 6701, and 6702 (sec. 113 of H.R. 6300)

Present law

Under present law, the burden of proof is on the Secretary in any proceeding in which the issue is whether an income tax return preparer has willfully attempted to understate the liability for tax of any person (*i.e.*, violated section 6694(b)).

H.R. 6300

H.R. 6300 would provide that the burden of proof would be on the Secretary in imposing the tax shelter promoter penalty (sec. 111 of H.R. 6300), the civil penalty for assisting in presentation of false documents (sec. 122 of H.R. 6300), and the penalty for frivolous returns (sec. 123 of H.R. 6300). The deficiency procedures would not apply to any of these penalties. Instead, provision is made for District Court review of the assessment after the taxpayer pays 15 percent of the penalty. This is generally the same procedure used in the return preparer area.

H.R. 5829

No provision.

C. Fraud, False Documents, Frivolous Returns

1. Fraud penalty (sec. 121 of H.R. 6300)

Present law

If any portion of an underpayment of tax is due to fraud, present law imposes a civil penalty (as an addition to tax) equal to 50 percent of the entire underpayment. If part of an underpayment is attributable to negligence or intentional disregard of rules and regulations, the penalty under present law is equal to 5 percent of the entire underpayment plus 50 percent of interest payable on the portion of the underpayment attributable to negligence or intentional disregard of rules and regulations for the period beginning on the last date prescribed for payment of the tax and ending on the date of assessment of the tax.

In the case of the windfall profit tax, both the negligence and the fraud penalty may apply to the same underpayment.

H.R. 6300

H.R. 6300 would increase the civil penalty for an underpayment of tax which is due at least in part to fraud by providing that in addition to the 50 percent penalty on the entire underpayment, there would be a penalty equal to 50 percent of the interest payable on the portion of the underpayment attributable to fraud for the period beginning on the last date prescribed for payment of the tax (without regard to any extension), and ending on the earlier of the date of assessment or the date of payment of the tax. This increase to the fraud penalty would parallel the increase in the negligence penalty enacted in the Economic Recovery Tax Act of 1981. Under the bill, the negligence penalty would not apply in any case in which the fraud penalty has been assessed.

The amendment would apply to taxes the last day for payment of which is after the date of enactment.

H.R. 5829

No provision.

2. Penalties for documents understating tax liability (sec. 122 of H.R. 6300 and sec. 121 of H.R. 5829)

Present law

Present law provides a criminal penalty for willfully aiding, assisting in, procuring, counseling, or advising the preparation or presentation of a false or fraudulent return, affidavit, claim or other document under the internal revenue laws. The criminal penalty is a fine of up to $5,000 or 3 years imprisonment, or both. There is no comparable civil penalty on persons who aid or assist in the preparation or presentation of false or fraudulent documents. However, income tax return preparers who willfully understate the liability for tax of any person are subject to a penalty of $500 per return.

H.R. 6300

H.R. 6300 would provide for a new civil penalty on any person who aids, assists in, procures, or advises, the preparation or presentation of a return, affidavit, claim or other document under the internal revenue laws which the person knows will likely be used in connection with any matter arising under the tax laws, and which the person knows will (if used) result in an understatement of the tax liability of another person. This penalty, which would be $1,000 for each return or other document ($5,000 in the case of returns and documents relating to the tax of a corporation) could be imposed whether or not the taxpayer knew of the understatements. The penalty could be imposed only once for any year with respect to the offender's actions in assisting any one person. Thus, someone who assists two individuals in preparing false documents would be liable for a $2,000 penalty where as the penalty would be only $1,000 if he had advised on two false documents for the same taxpayer. The burden of proof in imposing the penalty would be on the Secretary. The return preparer penalties would not apply to any person with respect to a return or claim for refund, if the new penalty for documents understating tax is imposed on that person with respect to that return or claim. However, this penalty would apply in addition to all other penalties provided by law. This penalty would apply beginning on the day after the date of enactment.

H.R. 5829

The penalty provision of H.R. 5829 relating to aiding in the presentation of a false return by a third party differs from that in H.R. 6300 both in the scope of covered offenses and in the measure of the penalty. The scope of H.R. 5829 is (1) narrower than that of H.R. 6300 in that it applies only to acts of corporate directors, officers, employees, and advisors that affect the corporation's tax, and (2) broader than that of H.R. 6300 in that it applies to any fraud that results in an understatement of the corporate tax. There is no requirement that the fraud be connected to the presentation or preparation of a return or other document under the internal revenue laws. The penalty under H.R. 5829 is equal to 50 percent of any corporate underpayment that results from the fraud (up to a limit of $100,000 per participant). Thus, the penalty varies in proportion to the harm done to the United States and not in proportion to the gain derived by the fraudulent director, etc.

3. Penalty for frivolous returns (sec. 123 of H.R. 6300)

Present law

Under present law, a taxpayer who files a protest return (such as one refusing to pay tax because the U.S. is no longer on the gold standard) may be subject to a penalty for failure to file a return. This penalty, however, is measured as a percentage of the underpayment of tax. Thus, if a taxpayer has paid the correct amount of tax through estimated tax or wage withholding, there is no penalty for filing a protest return. In addition, even when there is an underpayment, it may take several years of administrative and judicial proceedings before any penalty is imposed.

H.R. 6300

H.R. 6300 would provide for an assessible penalty of $500 on the filing of any document which purports to be a return of tax if (1) the document does not contain information from which the substantial correctness of the amount of tax shown on the return can be judged or contains information that on its face indicates that the amount of tax shown on the return is substantially incorrect, and (2) such conduct arises from a position taken by the taxpayer on the purported return which is frivolous, or from a desire to delay or impede administration of the Federal income tax laws. The penalty would be imposed, therefore, only on purported returns that are patently improper. Since it would be unnecessary to determine the taxpayer's true tax liability before imposing the penalty, H.R. 6300 would permit immediate assessment of the penalty. Assessment of the penalty would not affect the final tax determination. The deficiency procedures, under which the taxpayer would receive advance notice before assessment would not apply to this penalty. There is, however, provision for District Court review of the assessment (sec. 113 of H.R. 6300). The penalty would be in addition to all other penalties provided by law and would apply to documents filed after the date of enactment.

H.R. 5829

No provision.

D. Administrative Summonses

1. Special procedures for third-party summonses (sec. 131 of H.R. 6300)

Present law

Under present law, if an administrative summons is served on a third-party recordkeeper summoning that person to produce the records of the business transactions or affairs of a person other than the person summoned, then notice of the summons must also be given to the person whose records have been summoned (the taxpayer) within 3 days of the day on which the summons was served. Such notice must be accompanied by a copy of the summons served and must contain directions on how the taxpayer can stay compliance with the summons. For these purposes, a third-party recordkeeper is a bank or similar financial institution, a consumer reporting agency, a credit card company, a brokerage house, an attorney, or an accountant.

The taxpayer can stay compliance with a third-party summons if the taxpayer notifies the recordkeeper in writing within 14 days not to comply with the summons and mails a copy of this notice to the Secretary by registered or certified mail. To enforce the summons, the Secretary must seek an order of a United States District Court compelling compliance, at which time the third-party recordkeeper or the taxpayer must assert its defenses for noncompliance. No examination of the summoned records can be made until the expiration of the period for notice not to comply or, if such notice is given, until the court authorizes examination.

H.R. 6300

Under H.R. 6300, a taxpayer, who is entitled to notice of the summons and who wishes to prevent compliance by the recordkeeper, would be required to begin a court proceeding to quash the summons within 20 days after notice of the summons was given. When a court proceeding is initiated, the taxpayer would be required to mail (by registered or certified mail) a copy of the petition to the recordkeeper and the Secretary. In the same court proceeding, the Secretary could seek to compel compliance with the summons. The recordkeeper would have the right to intervene in the proceeding to quash the summons, and would be bound by any decision in such proceeding, even if it did not intervene. No examination of the summoned records would be allowed before the close of the twenty-third day after notice of summons was given, or if a proceeding to quash was begun, until the court so ordered. The bill also expands the definition of third-party recordkeepers to include barter exchanges. The amendment would apply to summonses served after December 31, 1982.

H.R. 5829

No provision.

2. Duty of third-party recordkeeper (sec. 132 of H.R. 6300)

Present law

Under present law, a third-party recordkeeper is bound to respond to a valid summons for records relating to a taxpayer unless the taxpayer stays compliance by notifying the recordkeeper not to comply

within 14 days of receipt of notice of the summons. A result of this procedure is that a third-party recordkeeper may be hesitant to start assembling the taxpayer's records or to comply with the summons until it is absolutely certain that the taxpayer has not sought to stay compliance.

H.R. 6300

H.R. 6300 would require third-party recordkeepers to proceed to assemble requested records upon receipt of the summons and to be prepared to produce the records on the date specified for their examination. Thus, the recordkeeper would not be permitted to wait until after the 20-day period in which the taxpayer would have the right to seek to quash the summons before assembling the summoned records. After expiration of a 23-day period, the bill would permit the Secretary to certify to the recordkeeper that no proceeding to quash had been initiated. Any recordkeeper who made a disclosure of records pursuant to a court order or in reliance on the Secretary's certification that no proceeding to quash had been commenced would not be liable to the taxpayer for the disclosure. The provision would take effect on the day after enactment.

H.R. 5829

No provision.

3. Limitation on use of administrative summonses (sec. 133 of H.R. 6300)

Present law

Present law has been interpreted as permitting the use of administrative summonses by the Internal Revenue Service only for the investigation of civil tax liabilities. Thus, the Supreme Court has ruled that the administrative summons is not available once the Internal Revenue Service has institutionally abandoned the investigation of civil tax liability, and has decided to pursue criminal prosecution of the case exclusively. The issue of whether the Service has decided to seek criminal prosecution has led to protracted litigation in many summons cases.

H.R. 6300

H.R. 6300 would provide a "bright-line" test for determining whether an administrative summons may be used. Such a summons could be used in any inquiry under the internal revenue laws as long as there had been no referral of the case to the Attorney General with a recommendation for criminal prosecution. The ability to use an administrative summons would be revived if the Attorney General notified the Internal Revenue Service that he declines to prosecute or that there has been a final disposition of the criminal proceeding. The amendment would take effect on the day after enactment. Each taxable period or event would be treated separately.

H.R. 5829

No provision.

II. IMPROVED INFORMATION REPORTING

A. Expanded Reporting

1. Transactions involving certain obligations (sec. 201 of H.R. 6300 and sec. 101(a) of H.R. 5829)

Present law

Under present law, any person making payments of interest, whether as principal or nominee, aggregating $10 or more in a calendar year, must file an information return with the Secretary and send an information statement to the interest recipient. Similarly, any corporation which has outstanding any evidence of indebtedness in registered form with respect to which there is $10 or more in original issue discount includible in the gross income of any holder in any calendar year must file a return with the Secretary stating the aggregate amount of the original issue discount so includible and send an information statement to such holder.

For purposes of this reporting requirement, "interest" is defined as interest on evidences of indebtedness of corporations issued in registered form, and to the extent provided for by regulation, interest on corporate bearer obligations of a type offered to the public; interest earned on bank deposits and on amounts paid by various financial institutions; interest paid on certain amounts held by insurance companies; and interest on deposits with stockbrokers and securities dealers. Interest does not include amounts paid on exempt governmental obligations, interest paid by or to certain foreign persons (to the extent provided by regulations), or amounts paid with respect to tax-free covenant bonds for which there is withholding. Likewise, by regulation, no payments of interest to or by the United States, a State, the District of Columbia, a foreign government, or a political subdivision of a State or foreign government, or an international organization need be reported. However, the Secretary is granted authority to require any corporation making a payment of interest, other than interest as defined above, to file such returns as the Secretary may require.

An obligation is "registered" for this purpose if it is registered as to both principal and interest (if any interest is payable) and if it can be transferred only by the surrender of the old instrument and (1) the reissuance of the old instrument to the new holder or, (2) the issuance of a new instrument to the new holder.

H.R. 6300

H.R. 6300 would expand both the categories of interest specifically subject to the information reporting requirements and the categories of persons liable to report such interest.

The bill would expand the definition of interest for information reporting purposes to include interest on any evidence of indebtedness issued in registered form or on any other obligation of a type offered

to the public (other than any evidence of indebtedness with a maturity of less than 1 year, which is held by a corporation). In addition to the other exceptions under present law, interest would not include any amounts paid by any natural persons.

In addition, H.R. 6300 would expand the reporting requirement with respect to original issue discount by providing that, for purposes of the information reporting provision, any original issue discount includible in the gross income of any holder of a corporate obligation would be treated as a payment by the corporate issuer of such original issue discount in that calendar year, whether or not the obligation is in registered form. The amount treated as paid would be equal to the entire amount of the original issue discount accruing during the calendar year without reduction for any amortization of the excess of the purchase price of the evidence of indebtedness paid by any transferee over the transferor's adjusted basis. The Secretary would also be authorized to prescribe regulations under which a payor would be required to report interest on a transactional, rather than an aggregate annual basis. Under such regulations, interest or OID on bearer obligations could be reported at maturity. Also, reporting would be required with respect to State and local obligations issued after December 31, 1982, unless such obligations were issued in registered form.

Finally, the bill would require that any person, including any governmental unit agency or instrumentality thereof, any corporation, trust, estate, or partnership, but not including any natural person, file such returns as the Secretary may require by regulation, regardless of the amount paid. In addition, the bill would provide that, to the extent provided in regulations, any financial institution, broker, or other person who collects interest for a payee (or acts as a payee's middleman), would be obligated to file any information return and information statement due on the transaction; no other person would have a reporting obligation with respect to any such payment.

Generally, these provisions would be effective after December 31, 1982.

H.R. 5829

H.R. 5829 would amend both the term "interest" for information reporting purposes, and the information return requirements. First, H.R. 5829 would provide that "interest" includes a corporate debt, whether or not registered, and interest on obligations of the United States, or any agency or instrumentality thereof. This expanded definition parallels the H.R. 6300 definition of interest. H.R. 5829 would also require reporting by any corporation, or the United States (an agency or instrumentality thereof) with respect to any original issue discount aggregating $10 or more includible in the gross income of any holder of such a person's obligation. This rule also parallels the rule of H.R. 6300. Although H.R. 5829 would apply to returns due after December 31, 1982, the provisions of H.R. 6300 would, in general, be effective with respect to interest paid after December 31, 1982.

2. Returns of brokers (sec. 202 of H.R. 6300 and sec. 101(b) of H.R. 5829)

Present law

Present law requires that every person doing business as a broker make a return, when required under regulations issued by the Secre-

tary, showing customer names, and such details regarding profits and losses, and such further information as the Secretary may require. There are, currently, no regulations issued under this section.

H.R. 6300

Under H.R. 6300, the rules relating to information returns would be revised. First, H.R. 6309 would provide that brokers required to file returns with the Secretary must also furnish a statement to each customer setting forth the broker's name and address and such other information as is required to be shown on the statement, on or before January 31 of the calendar year following the calendar year with respect to which the return is filed. This statement would serve to recapitulate for the customer the transactions engaged in by him during the previous calendar year and would aid the customer in filing an accurate income tax return.

Second, H.R. 6300 would define the term "broker" to include dealers and any other persons who regularly act as middlemen for profit with respect to transactions in property, as well as barter exchanges. This definition would not include persons, such as wholesalers, who act for their own account.

Finally, it would be anticipated that the Secretary would prescribe new regulations at least with respect to security and commodities brokers and dealers as soon as it is practicable. These regulations would require reporting of gross proceeds, and also may require details regarding profits and losses and other information where appropriate.

This provision would be effective on the date of enactment. However, to assure that the persons affected by the new filing requirements could prepare to comply, the regulations issued under this provision would not take effect until after 1982.

H.R. 5829

H.R. 5829 would not amend the provisions of the Code relating to broker reporting; instead, the Secretary would be instructed to issue regulations under existing law to require reporting by securities and commodities brokers. Thus, H.R. 5829 would not modify the definition of broker nor require that information statements be furnished to the taxpayer with respect to whom a return is made.

3. Information requirements for payments to nonemployees (sec. 203 of H.R. 6300)

Present law

Present law generally requires persons who are engaged in a trade or business to file information returns with respect to payments to other persons, in the course of such trade or business, aggregating $600 or more in the taxable year. This reporting obligation, subject to various exceptions, applies to payments of salaries, wages, commissions, fees, other forms of compensation for services, and other fixed or determinable gains, profits, or income. These information returns generally must contain the name, address, and identification number of the recipient of the payment, and the aggregate amount paid. Persons subject to this reporting requirement must provide the recipient of the payments with a statement showing the payor's name, address, and identification number, and the aggregate amount paid.

H.R. 6300

H.R. 6300 would provide a separate reporting requirement for payments to persons who are not employees and would impose a new reporting requirement with respect to certain direct sales. Under the bill, a person engaged in a trade or business who pays amounts in the course of that trade or business to any person (payee) for services performed would have to file with the Internal Revenue Service an information return reporting such payments (and the name, address, and identification number of the payee) if the payments during the calendar year were $600 or more. Also, the payee would have to be furnished with a statement setting forth the name, address, and identification number of the person making the return, and the aggregate amount of the payments.

In addition, H.R. 6300 would provide a new information reporting requirement for certain direct sellers. The new requirement would apply if a person, in the course of a trade or business, sells products aggregating $600 or more to any buyer engaged in selling such products on a direct-sale basis or selling such products to other persons so engaged. In general, the person making the sale would have to file an information return setting forth the aggregate amount of the sales to the buyer and the name, address, and identification number of the buyer. The buyer would be furnished with a statement setting forth the name, address and identification number of the seller, and the aggregate amount of sales to the buyer.

A resale of products would be on a direct-sale basis, and, thus, subject to the bill's new information reporting requirements, if the resale is on a buy-sell basis, a deposit-commission basis, or similar basis specified in Treasury regulations, and in a home or otherwise than in a permanent retail establishment. A transaction would be on a buy-sell basis if the seller is entitled to retain part or all of the difference between the price at which he purchases the product and the price at which he sells the product as his remuneration for the transaction. A transaction would be on a deposit-commission basis if the seller is entitled to retain part or all of the deposit paid by the customer in connection with the transaction as his remuneration for the transaction.

Failures to comply with these information reporting requirements would be subject to the generally applicable penalty provisions relating to information returns present in the Code (as revised by sections 211–213 of H.R. 6300). Specifically, for purposes of the backup withholding provisions (sec. 213) of H.R. 6300, any person making a sale on a direct-sale basis would be treated as having made a payment to the buyer equal to the value of the goods sold.

The new information reporting requirements would apply in calendar years beginning after 1982.

H.R. 5829

No provision.

4. State and local income tax refunds (sec. 204 of H.R. 6300 and sec. 102 of H.R. 5829)

Present law

Refunds of State or local income taxes that were deducted in a previous taxable year are includible in a taxpayer's gross income to the

extent the deduction gave rise to a tax benefit. Under present law, there is no requirement that information returns for such refunds be filed with the United States or that refund recipients receive information statements on such refunds during the tax-filing season.

H.R. 6390

H.R. 6300 would require that information returns for State and local income tax refunds, credits, or offsets aggregating $10 or more, paid to any individual, be filed with the Internal Revenue Service. Such return would report the aggregate amount of any such refund payments, credits or offsets, and the recipient's name and address. It would be anticipated that States and local governments could satisfy the return obligations through voluntary information exchange agreements such as those now currently in effect between the United States and several States. A statement with respect to each return would have to be furnished to the recipient of the refund during January of the calendar year following the calendar year in which the refund is made. This new requirement would apply to refunds, credits, and offsets made after December 31, 1982.

H.R. 5829

This provision of H.R. 5829 is substantially similar to that in H.R. 6300 except that H.R. 6300 is limited to reporting on the refunds, credits, or offsets to individuals while H.R. 5829 requires reporting on refunds, credits, or offsets to any person, including corporations, trusts, and estates, etc.

5. Casualty reimbursements (sec. 205 of H.R. 6300)

Present law

Present law allows an individual to deduct personal losses (in excess of $100) sustained during the taxable year that arise from fire, storm, shipwreck, or other casualty, or from theft, if such losses are not compensated for by insurance or otherwise.

Under present law, there is no requirement that persons paying compensation for casualty losses file information returns with respect to such reimbursements with the Service, nor that information statements be furnished to the recipients of the reimbursements.

H.R. 6300

H.R. 6300 would subject reimbursements for casualty and theft losses to the general information reporting at source requirements, under section 6041(a). An information return would be required for a reimbursement of $600 or more; likewise, an information statement would be required to be furnished to the recipient of the reimbursement. The provision would be effective for payments made after December 31, 1982.

H.R. 5829

No provision.

6. Reporting of charged tips (sec. 103 of H.R. 5829)

Present law

Under present law, an employee who receives tips in excess of $20, in cash or its equivalent, in the course of his employment must report all such tips in a monthly statement furnished to his em-

ployer. The employer must generally take these tips (but no others) into account in determining the amount of tax to be withheld from the employee's wages. No other reporting requirements are imposed on employers with respect to tips.

H.R. 6300

No provision.

H.R. 5829

Under H.R. 5829, any employer (other than a small employer) who pays over to an employee $600 or more of charged tips in any taxable year would be required to report those tips to the Internal Revenue Service. Withholding on these charged tips (to the extent not paid over to other employees under pooling arrangements) would be required, as under present law, when the employee reports them together with other tip income to the employer. The amount reported by an employee on his tax return may be different, of course, from that reported by the employer because of pooling and other tip sharing arrangements. Small employers, who are defined as persons who normally have employed five or fewer employees during the previous calendar year, would be exempt from this reporting requirement. The new rules would apply to charge tips paid over to employees after December 31, 1982.

B. Provisions to Improve Reporting Generally

1. Increased penalties for failure to file information returns (sec. 211 of H.R. 6300 and sec. 124(a) of H.R. 5829)

Present law

Present law imposes a penalty on any person who fails to file, on the date prescribed (with extensions), information returns, including returns relating to certain information at source involving payments of $600 or more, payments of dividends aggregating $10 or more, payments of patronage dividends aggregating $10 or more, payments of interest aggregating $10 or more, payments of certain fishing boat operators, income tax withheld, or payments of wages in the form of group-term life insurance. The penalty is $10 for each such failure, but the total for all such failures during a calendar year cannot exceed $25,000. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect.

H.R. 6300

H.R. 6300 would increase the penalty for failure to file the information returns noted above to $50 per failure, the total amount for all such penalties for any calendar year not to exceed $50,000. The bill would provide a new penalty for failures due to intentional disregard of the filing requirements. In such circumstances, the penalty would not be less than 10 percent of the aggregate amount of the payments not properly reported. Finally, the bill would expand the category of returns covered by these provisions to include returns for payments to nonemployees (sec. 203 of H.R. 6300) and payments to customers by brokers and dealers (Code sec. 6045).

This provision would apply to all returns the due date of which (without regard to extensions) is after December 31, 1982.

H.R. 5829

The provision is generally the same except that the second tier penalty for international disregard of the filing requirements would be 5 percent (instead of 10 percent) of the aggregate amounts not properly reported in the case of reports from brokers.

2. Minimum penalty for extended failure to file (sec. 122 of H.R. 5829)

Present law

Under present law, if a taxpayer fails to file a tax return on the date prescribed (with extensions of time for filing), a penalty is imposed based on the amount of any underpayment of tax for the year. The penalty is 5 percent of the underpayment per month, or fraction thereof, while the failure continues, but not more than 25 percent in the aggregate. Thus, no penalty is imposed on the taxpayer if there is no underpayment for the year or if a refund is due. Likewise, no penalty is imposed if the failure is due to reasonable cause and not due to willful neglect.

H.R. 6300

No provision.

H.R. 5829

H.R. 5829 would add a new minimum penalty for the extended failure to file any income tax return. If an income tax return is not filed within 60 days of the date prescribed (with extensions), the penalty for failure to file would not be less than $100. Also, this minimum penalty would not be imposed if the failure to file the return was due to reasonable cause and not due to willful neglect. The penalty would apply to returns due after December 31, 1982.

3. Increase in civil penalty on failure to supply identifying numbers (sec. 212 of H.R. 6300 and sec. 124(b) of H.R. 5829)

Present law

Present law imposes a penalty of $5 per failure on any person who is required by regulations (1) to include his taxpayer identification number (TIN) in any return, statement or document; (2) to furnish his TIN to another person; or (3) to include in any return or statement made with respect to another person the TIN of such other person; and who fails to comply with such requirement at the time prescribed. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect. In practice, this penalty is rarely, if ever, imposed.

H.R. 6300

H.R. 6300 would increase the $5 penalty to $10 with respect to the TIN requirement, in case (1), and to $50 in cases (2) and (3), above. This would be effective for returns the due date of which (without regard to extensions) is after December 31, 1982.

H.R. 5829

The provision is generally the same except that the penalty for the failure described by case (1) would be increased to $50 (rather than

$10). Also, there would be an overall limit on such penalties of $50,000 for any year.

In addition, if a failure as described by case (3) was due to the intentional disregard of the requirements to include a payee's TIN, there would be a penalty of $100 per failure, with no limit.

4. Extensions of withholding to certain payments where identifying number not furnished or inaccurate (sec 213 of H.R. 6300 and sec. 124(c) of H.R. 5829)

Present law

Present law imposes a penalty of $5 per failure on any person who is required by regulations to include his taxpayer identification number (TIN) in any return, statement, or document, to furnish his TIN to another person, or to include in any return or statement made with respect to another person the TIN of such other person, and who fails to comply with such requirement at the time prescribed. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect. Present law does not impose any withholding obligation on any payor making a payment subject to an information reporting requirement based on whether the payor has received a TIN, or a correct TIN, from a payee.

H.R. 6300

H.R. 6300 would provide for withholding at source at a tax rate of 10 percent if a taxpayer fails to supply a TIN or supplies an incorrect TIN to another person who must file certain types of information returns with respect to payments to the taxpayer. The types of payments subject to this withholding requirement would include payments of dividends and interest, and payments from brokers and certain dealers. The determination of whether such payments were subject to this withholding requirement would be made without regard to the minimum threshold amounts that apply for purposes of information reporting.

Also, this new withholding provision would apply to payments of rents, salaries, wages, commissions, fees, or other forms of compensation for services and other fixed or determinable gains, profits, or income, and certain payments to independent contractors or by direct-sellers, but only when (1) the aggregate amount of the payments to the payee during the calendar year equals or exceeds $600, (2) the payor was required in the preceding year to file an information return for such payee, or (3) the payor was required the preceding year to withhold on such payments to the payee.

Generally, payment of amounts subject to this new withholding provision would be treated as wages paid by an employer to an employee and subject to the various provisions applying to collection of income tax at the source on wages.

If the TIN is not supplied, the payor-filer would start withholding when any payments are made. If the TIN is incorrect, the payor would start withholding upon notice from the Secretary that the taxpayer has failed to supply the correct TIN. (A copy of such notice would also be required to be mailed to the taxpayer.) Generally, such with-

holding would continue as long as the taxpayer failed to supply or correct his TIN.

The bill would require the Secretary to provide for exemptions from the backup withholding provisions during periods in which a person is awaiting receipt of an identification number.

This provision would apply to payments made after December 31, 1983.

H.R. 5829

H.R. 5829 is similar to H.R. 6300 except that the withholding at source would be at a tax rate of 15 percent. Also, if the TIN is not supplied, the payor-filer would start withholding when aggregate payments to the taxpayer for the calendar year exceeded any threshold requiring the reporting of such payments. If the TIN is incorrect, the payor would start withholding upon notice from the Secretary that the taxpayer has failed to supply the correct TIN within 60 days after notice from the Secretary.

In addition, the withholding provisions in H.R. 5829 would apply to patronage dividends, payments of certain fishing boat operators, and payments of group-term life insurance, but would not apply to transactions of direct-sellers. H.R. 5829 does not require reporting with respect to direct sellers.

5. Criminal penalty for failure to pay estimated tax (sec. 123 of H.R. 5829)

Present law

Present law imposes a criminal penalty for willful failure to pay any estimated tax at the time required by law. A person convicted of such willful failure is guilty of a misdemeanor and may be fined not more than $10,000 or imprisoned not more than 1 year (or both), together with costs of prosecution. Such penalty may apply even if no civil penalty can be assessed.

H.R. 6300

No provision.

H.R. 5829

H.R. 5829 would provide that any person who fails to make any estimated tax payment would not be subject to the criminal penalty for such failure if the civil penalty for failure to pay estimated tax is not applicable.

6. Form of information returns (sec. 211 of H.R. 6300 and sec. 101 of H.R. 5829)

Present law

In general, returns required by the tax laws must be made according to the forms and regulations prescribed by the Secretary. As a general rule, these returns must be in written form except that in certain cases the return may be made by filing the required information on magnetic tape or other medium, provided that the prior consent of the Commissioner is obtained. There is no statutory or regulatory requirement that any particular return be filed on magnetic tape or in other machine-readable form.

H.R. 6300

H.R. 6300 would require the Secretary to prescribe regulations providing standards for determining which returns must be filed in machine-readable form (e.g., on magnetic tape or on paper forms susceptible to optical character scanning). In prescribing these regulations, the Secretary would be required to take into account the cost, among other factors, of the filing requirement to the taxpayer.

H.R. 5829

The provision is generally the same except that the Secretary is not explicitly required to consider the cost to the taxpayer when requiring returns to be submitted in machine-readable form.

III. PENSIONS AND OTHER RETIREMENT INCOME

A. Withholding Provisions

1. Withholding on pensions, annuities, and certain other deferred income (sec. 301 of H.R. 6300 and sec. 131 of H.R. 5829)

Present law

Under present law, income tax generally is not required to be withheld from benefits paid under a tax-qualified pension, profit-sharing, or stock bonus plan, under a tax-sheltered annuity program or under an IRA (an individual retirement account or annuity or a U.S. retirement bond). Also, payments under a commercial annuity contract generally are not subject to withholding. However, tax is required to be withheld on an annuity payment if a voluntary withholding request by the recipient is in effect.

H.R. 6300

Withholding required

Under H.R. 6300, tax would generally be withheld from all designated distributions (the taxable part of payments made from or under a pension, profit-sharing, stock bonus, or annuity plan, a deferred compensation plan where the payments are not otherwise considered wages, an IRA, or a commercial annuity contract). The withholding rate would be determined by the nature of the distribution. Tax would be withheld on periodic payments (typically, annuity payments) as if those payments were wages paid by an employer to an employee for the appropriate payroll period (subject to the usual rules for personal and other exemptions from withholding). It is anticipated that the Secretary of the Treasury would provide guidance to determine the appropriate payroll period. Withholding would not be required with respect to the first three months of periodic payments, although the payor and payee could agree to earlier withholding.

For nonperiodic distributions, tax generally would be withheld at a 10 percent rate. In the case of total distributions under qualified pension, etc., plans (sec. 401(a) or 403(a)), tax would be withheld under special rules designed to reflect the 10-year forward income averaging and capital gains treatment provided for lump sum distributions. It is anticipated that Treasury regulations will describe the circumstances in which it is reasonable to believe that the income tax exclusion for employer-provided death benefits will be allowable. To the extent provided by such regulations, the exclusion would be taken into account in determining the withholding tax.

Elections

Under H.R. 6300, recipients could elect not to have the withholding rules apply. For periodic payments, an election would be effective until revoked. In the case of nonperiodic distributions (including total dis-

tributions under qualified plans), an election not to have income tax withheld generally would be required for each such distribution. However, the bill would allow a recipient's election to apply to more than one nonperiodic distribution from the same payor to the extent provided by Treasury regulations. For example, regulations could permit an annual election to have no tax withheld from amounts paid from an individual retirement account during a year.

Payors would be required to notify recipients of the right to elect not to have the withholding rules apply. For periodic payments, the notice would be required not earlier than 2 months before the date of the first payment, and not later than the date of the first payment. For purposes of the withholding rules relating to periodic payments, if the payments are suspended (for example, by reason of a retiree's return to the service of the employer), the first periodic payment made after the suspension would be treated as a first periodic payment. In addition, the bill would require that payors of periodic payments notify payees at least once each year of the right to make or revoke the withholding election.

With respect to a nonperiodic distribution, the bill would require the payor to provide notice of the right to elect not to have income tax withheld at the time of the distribution. The bill also would permit Treasury regulations to require earlier notice by the payor in certain cases. For example, unless recipients of lump sum distributions are notified of their rights to elect not to have withholding apply before they receive their distributions, they may be unable to transfer the full amount eligible for a tax-free rollover. In order to prevent this result it is anticipated that Treasury regulations will require that recipients of total distributions from qualified plans be informed before plan distributions are made of their right not to have withholding apply. In order to provide participants with a reasonable time in which to make this election, it is anticipated that this notice will generally be required to be provided no more than 90 days and no less than 30 days before the time of the distribution.

Coordination with other provisions

The rules of the bill for designated distributions would not apply to amounts paid as wages subject to the usual wage-withholding rules. In addition, the rules of present law for income tax withheld from wages would apply to amounts withheld from designated distributions. With respect to designated distributions, the bill would replace the provisions of present law which permit voluntary withholding on amounts paid as an annuity.

Reports

To improve compliance, the bill would provide for reporting of necessary information by employers, plan administrators, and issuers of insurance or annuity contracts. The reports would include the name, address, taxpayer identification number, and certain other information with respect to each payee who elects not to have the withholding rules apply. As under present law, penalties would apply to any person failing to provide a required report, unless the failure was determined to be due to reasonable cause and not due to willful neglect. The form and manner of reporting would be determined under regulations prescribed by the Secretary of the Treasury.

The bill also would provide a new penalty if the data base needed for reports is not maintained. The penalty would apply whether or not reports are due for the period during which the recordkeeping occurs. No penalty would be imposed for failure to meet the recordkeeping rules when the failure is due to reasonable cause and not willful neglect. Also, no penalty would be imposed for a recordkeeping failure that is due to a prior failure with respect to which the penalty has already been imposed or which occurred before 1983, if all reasonable efforts have been made to correct the prior failure.

Effective dates

In general, the withholding rules would apply to designated distributions made after December 31, 1982. For purposes of applying the rules to periodic payments which commenced prior to January 1, 1983, the first periodic payment after December 31, 1982, is considered the first periodic payment made. Thus, no withholding would be required with respect to any periodic payment made before April 1, 1983. The reporting requirements and voluntary withholding rules would be effective on January 1, 1983, and the recordkeeping penalties would be effective on January 1, 1985.

H.R. 5829

Withholding required

H.R. 5829, like H.R. 6300, subjects certain pension and annuity payments to withholding taxes, with the rate of withholding to be determined by the nature of the distribution. Unlike H.R. 6300, however, the bill would separate payments into only two classes: qualified distributions (subject to wage withholding) and qualified total distributions (subject to special rules designed to reflect the 10-year forward averaging rules and capital gains treatment provided for lump sum distributions).

Elections

Under H.R. 5829, a recipient of a qualified distribution which was not a total distribution could elect (for any reason) not to have the withholding rules apply. H.R. 5829, unlike H.R. 6300, would require that this election be renewed annually.

With respect to total distributions, H.R. 5829 permits a recipient to elect out of the withholding system only if the recipient provides notice that the distribution will be rolled over, tax-free, to another qualified plan, or to an IRA.

H.R. 5829 also provides special rules to permit a recipient who rolls over a total distribution to separately roll over any amounts withheld. If the recipient (before August 15 of the calendar year following the distribution) takes such action as the Secretary may prescribe to treat the amount of tax withheld as a rollover, that amount would not be includible in the recipient's gross income.

H.R. 5829, like H.R. 6300, requires that payors notify recipients of the right to elect not to have the withholding rules apply, but H.R. 5829 authorizes the Treasury to issue regulations prescribing the timing of such notice.

Coordination with other provisions

Under H.R. 5829, it is intended that the rules of present law for income tax withheld from wages apply to amounts withheld from quali-

fied distributions. H.R. 5829, unlike H.R. 6300, would repeal the provisions of present law which permit voluntary witholding on amounts paid as an annuity.

Reports

H.R. 5829 would require reports only from employers and plan administrators and would leave the form and timing of such report to Treasury regulations. No new penalties would be imposed for failure to maintain adequate records.

Effective date

H.R. 5829 would apply with respect to payments made after December 31, 1982.

B. Provisions Relating to Individual Retirement Accounts

1. Increase in penalty for premature distributions (sec. 311 of H.R. 6300)

Present law

Present law provides for a 10-percent excise tax on certain early distributions from an IRA, from accumulated deductible employee contributions or from an H.R. 10 plan. Generally, an early distribution is one made before age 59½, unless it is made on account of death or disability.

H.R. 6300

H.R. 6300 would increase the rate of the excise tax on early distributions from 10 to 15 percent. The increase would apply to distributions made after December 31, 1982.

H.R. 5829

No provision.

2. Partial rollovers of IRA distributions permitted (sec. 312 of H.R. 6300)

Present law

Under present law, distributions from an IRA are eligible for tax-free rollover treatment only if the entire amount of the distribution is rolled over to another eligible retirement plan. In contrast, distributions from qualified plans are eligible for tax-free rollover treatment to the extent of any amount so transferred.

H.R. 6300

H.R. 6300 would allow similar partial rollovers for IRA distributions made after December 31, 1982.

H.R. 5829

No provision.

IV. TRANSACTIONS OUTSIDE THE UNITED STATES

A. Access to Records

1. Jurisdiction of court and enforcement of summons in the case of persons residing outside the United States (sec. 401 of H.R. 6300)

Present law

Under present law, an administrative summons may be directed to a U.S. person outside the United States. However, it may not be enforceable because section 7604 and other operative sections of the Code fail to specifically confer venue to enforce the summons on a District Court except when a person "resides or is found" in a judicial district of the United States. Because a U.S. citizen or resident living abroad may not reside in or be found in a judicial district of the United States there may be no district court that can enforce a summons served on such a person.

H.R. 6300

In these situations, H.R. 6300 would establish venue for summons enforcement actions involving U.S. citizens or residents living abroad in the United States District Court for the District of Columbia. This would be accomplished by treating a citizen or resident of the United States who does not reside in any U.S. judicial district, and who is not found in any U.S. judicial district, as residing in the District of Columbia for tax purposes relating to jurisdiction of courts and enforcement of summons.

This provision would be effective on the day after the date of enactment.

H.R. 5829

No provision.

2. Treatment of foreign transactions with respect to which there are not adequate books and records (sec. 402 of H.R. 6300)

Present law

Under present law, in general, the burden of proof in tax matters is on the taxpayer. He is required to submit evidence sufficient to establish his deductions or the tax effects of transactions. Taxpayers have an obligation to maintain adequate books and records, and are required to maintain such books and records as the Secretary requires (section 6001). Special rules require U.S. shareholders of controlled foreign corporations to maintain books and records relating to transactions of those corporations (section 964).

Despite these rules, the Internal Revenue Service has had problems dealing with foreign transactions. These problems have arisen in the context of illegal income as well as legitimate business transactions.

For example, one common method employed by U.S. persons to launder drug profits is to carry the cash to a tax haven, deposit it with a small bank, and then have the bank lend the proceeds back to the dealer. The loan is fully documented. The IRS might try to assert a deficiency against the dealer. However, a properly documented phony loan transaction can make such a deficiency difficult to sustain.

At times, taxpayers engaged in manipulative transactions overseas may refuse to provide books and records to an IRS agent, or use delaying tactics in the hope of getting a better settlement. They will not produce the documentation until they are in court when it is more difficult to fully examine the transactions. Often, tax haven bank or commercial secrecy laws carrying criminal penalties for violation are cited as the reason for failing to produce the requested information. Also, numerous cases have occurred where taxpayers engage in transactions with foreign financial institutions which they claim are not related to them, when, in fact, they may control the institution or the funds being used.

H.R. 6300

H.R. 6300 would generally restrict a taxpayer, who has refused to provide items of documentation of foreign transactions requested by the Internal Revenue Service during audit, from using the requested documentation to prove his view of those transactions in court. This would be accomplished by requiring any court having jurisdiction over the issue to prohibit the introduction by the taxpayer of any foreign-based documentation covered by a document request relating to the item unless that documentation was provided to the Internal Revenue Service within the time provided in the bill.

An exception to the general rule would be provided if the taxpayer establishes to the satisfaction of the court that the failure to provide the documentation when requested was due to reasonable cause. Under the bill, the fact that providing the information violates local law is not reasonable cause. Thus, it would be more difficult for the taxpayer to establish reasonable cause when requested documentation is in a tax haven.

The bill would also create a presumption that any amount received from a foreign jurisdiction is income (rather than, for example, a loan) unless, upon request of the Internal Revenue Service, the recipient produces sufficient documentary evidence that establishes that the amount is not income. Likewise, there would be a presumption that any tax benefit purporting to arise in a foreign country would be denied unless, on request of the Internal Revenue Service, sufficient documentary evidence were provided to establish the true nature of the transaction.

The bill would establish safeguards so that the taxpayer would have adequate notice and adequate time to produce requested documentation. The bill provides for a 90-day period (or longer, if allowed by the Secretary) to comply with a request. It is anticipated that the Secretary would extend the time limit for compliance where, for example, local procedures which take a relatively short additional period of time can be followed by the taxpayer to obtain the requested documentation. Also, the Commissioner would have to describe the requested information in some detail, and would have to state with

specificity the reason why what has been produced by the taxpayer already is not adequate.

The bill would also provide that if the admissibility of evidence provision, the presumption that a foreign item is income, or the denial of a tax benefit provision, apply to a taxpayer because of a request for information arising out of any trade or business (or other activity) of the taxpayer, then the Secretary may require that the taxpayer maintain documentation for the trade or business in the United States, at a place designated by the Secretary. This provision would not apply if a court determines that the taxpayer's failure to produce the requested information was due to reasonable cause.

This provision would be effective for formal document requests mailed after the date of enactment.

H.R. 5829

No provision.

B. Information Returns

1. Penalty for failure to furnish information with respect to foreign corporations (sec. 411 of H.R. 6300)

Present law

Under present law, a U.S. person who controls a foreign corporation is required to furnish the Internal Revenue Service with tax-related financial and shareholder information concerning the corporation (section 6038(a)). The Secretary is authorized to prescribe regulations setting forth the specific information to be furnished. The penalty for failure to furnish the required information is a 10 percent reduction of the U.S. person's foreign tax credit. Additional five percent reductions are provided for continued failures to file.

Despite complaints about inadequate reporting of transactions of controlled foreign corporations, penalties generally are not imposed. (section 6038(b)). In part this is because the penalty is complicated. It also may be unduly harsh in some cases.

H.R. 6300

H.R. 6300 would simplify the penalty for failure to furnish information with respect to a controlled foreign corporation by adding a fixed dollar penalty for failure to furnish the required information. The penalty would be $1,000 for each failure to furnish information for each annual accounting period (generally a taxable year) of the foreign corporation. If the failure continues for more than 90 days after notification by the Secretary, then there would be additional $1,000 penalties for each 30-day period (or fraction thereof) during which the taxpayer continues to fail to produce the requested information.

The bill would give Internal Revenue Service agents a simple straight-forward penalty to impose where reports with respect to controlled foreign corporations are not filed or are inadequate. However, it would retain the potentially significant penalty of a reduction in foreign tax credit to be imposed where the Internal Revenue Service considers it appropriate. Where both penalties were applied, the amount of the reduction in the foreign tax credit would be reduced by the amount of the fixed dollar penalty imposed.

There would be no change in the present law substantive reporting requirements.

This provision would be effective for annual accounting periods ending after the date of enactment.

H.R. 5829

No provision.

2. Returns with respect to foreign personal holding companies (sec. 412 of H.R. 6300)

Present law

Under present law, each person who is an officer or director of a foreign personal holding company, and each 50-percent or greater U.S. shareholder of a foreign personal holding company, is required to file certain reports with respect to that corporation (section 6035). Both monthly reports of stockholdings and annual reports of income are required. The monthly report of stock holdings in the corporation is due on the 15th day of each month for which a report is required, but the Secretary is authorized to delay the filing of this report to a due date that is on the 15th day of a later month. By regulations the Secretary has delayed the filing date and required filing after the close of the foreign corporation's taxable year. The report of the income of the foreign corporation must be filed within 60 days after the close of the taxable year of the foreign personal holding company to which it relates.

Today, the Internal Revenue Service requires persons engaging in international transactions, and persons who transfer assets to foreign entities, to file a number of different forms. Often, a person may have to file more than one form covering the same foreign entity for the year. The Internal Revenue Service would like to combine a number of these forms into one and generally require that it be filed after the close of the filer's taxable year. However, the filing dates tied to the date of a transaction for certain reports described below (section 413 of H.R. 6300), as well as the filing dates for reporting relating to foreign personal holding companies, make it impossible for these forms to be combined.

H.R. 6300

H.R. 6300 would change present law to make it possible for the Internal Revenue Service to include the foreign personal holding company reports in a combined international report. In particular, it would authorize the Commissioner to designate the time when the foreign personal holding company reports and returns must be filed.

In addition, the bill would clarify the information that must be included in a return. The persons required to file the reports would also be clarified. The bill would change present law by placing the reporting obligation on any 10-percent (rather than 50-percent) shareholder of a foreign personal holding company as well as on officers and directors. As under present law, ownership would include both direct and indirect ownership of stock.

Whether or not a person is required to file a return is determined on the date the return is required to be filed. If, on that date, no person would be required to file (because, for example, the corporation has been dissolved), then filing would be required by the persons who

were officers, directors or 10-percent shareholders on the last day of the corporation's taxable year for which there was a person required to file.

If more than one person would be required to file, the Secretary may, by regulations, require only one of them to file.

This provision would apply to taxable years of the foreign corporation beginning after the date of enactment.

H.R. 5829

No provision.

3. Delay in date for filing certain returns relating to foreign corporations and foreign trusts (sec. 413 of H.R. 6300)

Present law

Under present law, a return must be filed by U.S. persons who are officers or directors of certain foreign corporations and by U.S. persons who acquire at least a five-percent interest (or an additional 5-percent interest) in a foreign corporation (sec. 6046). The return must be filed within 90 days of the event that triggers the duty to file.

A return must also be filed by certain persons transferring property to a foreign trust, including a grantor or a fiduciary (sec. 6048). Once again, the return must be filed within 90 days of the triggering event, in this case creation of the trust or a transfer to the trust.

As described under the explanation of the foreign personal holding company reporting requirements (section 412 of the bill), the Internal Revenue Service is considering consolidating a number of international reporting forms. The specific reporting dates tied to a triggering event, rather than a taxable year, would make it impossible to include these reports relating to foreign corporations and trusts in the combined report.

H.R. 6300

H.R. 6300 would authorize the Commissioner of Internal Revenue to delay the reporting of the transactions covered by sections 6046 (foreign corporations) and 6048 (foreign trusts) until some date after the 90th date after the transaction. This would give the Commissioner the flexibility needed to include these reports in the combined foreign report.

This provision would apply to returns filed after the date of enactment.

H.R. 5829

No provision.

4. Technical amendment relating to penalty under section 905(c) (sec. 414 of H.R. 6300)

Present law

Under present law, if a foreign tax for which a U.S. foreign tax credit was taken is refunded the taxpayer must notify the Secretary of the refund (section 905(c)). The Secretary then redetermines the taxpayer's tax and notifies the taxpayer of the amount due. Interest on any additional tax does not begin to run until the taxpayer receives the refund of the foreign tax. This rule is in contrast to the general rule for payment of interest which is that interest is imposed on any

amount of tax that is due but not paid on the last date prescribed for payment (section 6601).

Section 2(c)(1) of the Act of December 28, 1980 added a sentence to section 905(c) that appears to provide that if a taxpayer does not notify the Commissioner of an adjustment in foreign taxes then interest on an underpayment of tax caused by an adjustment of the taxpayer's foreign taxes paid will begin to run from some point in time before the taxpayer received the refund of the foreign tax. This provision was intended to penalize a taxpayer for failing to notify the Commissioner of a refund of foreign taxes. However, it is ambiguous, and also unnecessary because the same Act that added it also added a penalty to the Code (section 6689) for failure to report a redetermination of foreign tax.

H.R. 6300

H.R. 6300 would repeal the last sentence of section 905(c), effective for years to which the Act of December 28, 1980 applies.

H.R. 5829

No provision.

V. COMPUTATION OF INTEREST

A. Interest to be Compounded (sec. 501 of H.R. 6300 and sec. 111 of H.R. 5829)

Present law

Under present law, interest payable to or by the United States under the tax law is not compounded.

H.R. 6300

Under H.R. 6300, all interest payable under the Internal Revenue Code would be compounded daily. This compounding requirement would apply beginning in 1983 to amounts remaining unpaid at the beginning of 1983 as well as all other interest accruing under the internal revenue laws after 1982.

H.R. 5829

H.R. 5829 would require interest to be compounded semi-annually instead of daily.

B. Restrictions on Payment of Interest on Certain Refunds, Etc. (sec. 502 of H.R. 6300 and sec. 133 of H.R. 5829)

Present law

In general, under present law, interest on refunds, credits and offsets runs from the date of overpayment, which is usually the date prescribed for filing the particular return. Further, under present law, if an overpayment of income tax is refunded within 45 days after the last date prescribed for filing the return, or if later, within 45 days after the date the return is filed, no interest is payable on the overpayment. An overpayment resulting from a net operating loss carryback, net capital loss carryback, or credit carryback (including a foreign tax credit carryback) is treated as having occurred at the close of the year in which the carryback arose.

H.R. 6300

Under H.R. 6300, no interest would be paid on a refund claimed on a late return if the refund is made within 90 days after the return is filed. Likewise, an overpayment resulting from a net operating loss carryback, a net capital loss carryback, or credit carryback (including a foreign tax credit carryback) would be treated as having occurred on the due date (with extensions) of the return for the year in which the carryback arose. Conforming amendments would be made in the rules relating to interest on underpayments. Under the bill, for purposes of the payment of interest on overpayments, a return would not be treated as filed until it is filed in processible form. The provisions regarding late returns and processible returns would be effective for returns filed after the 30th day after the date of enactment. The pro-

vision regarding interest overpayments due to carrybacks would be applicable to interest accruing after enactment.

H.R. 5829

H.R. 5829 would provide that no interest is due on an overpayment for any period prior to the later of the filing of the return or the due date (without extensions). For example, if an individual filed an income tax return claiming a refund on June 1 (rather than April 15), interest would run from June 1; however, if the refund were paid within 45 days no interest would be payable (as under present law). If the same taxpayer subsequently amended the June 1 return, interest on any refund claimed on the amended return would run from June 1 (rather than April 15 as in present law).

With respect to refunds arising from net loss carrybacks, H.R. 5829 would deny interest for any period prior to the date the refund is claimed or otherwise applied for. The amendment to the interest rules would apply to payments of interest accruing after March 11, 1982 if those payments are made later than 30 days after enactment. H.R. 5829 would not change the interest rule for foreign tax credit carrybacks.

Like H.R. 6300, H.R. 5829 would provide that a return is not treated as filed for purposes of the interest on refunds until the return is filed in a processible form.

C. Semiannual Determination of Rate of Interest (sec. 112 of H.R. 5829)

Present law

Under present law, the rate of interest to be paid on underpayments, on overpayments, and for other purposes, must be established by the Treasury no later than October 15 of any year, based on the average predominant prime rate (the rate quoted by commercial banks to their preferred customers for short-term loans) rounded to the nearest full percentage during September of that year, effective January 1 of the following year.

H.R. 6300

No provision.

H.R. 5829

Under the bill, interest rates would be determined semiannually and would be based on the average adjusted prime rate charged by commercial banks during the six-month period ending September 30 (effective January 1 of the succeeding calendar year), and March 31 (effective July 1 of the same calendar year). The amendment would be effective for adjustments taking effect after December 31, 1982.

D. Nondeductible Interest Surcharge for Substantial Understatement (sec. 503 of H.R. 6300 and sec. 125 of H.R. 5829)

Present law

Under present law, a penalty is imposed on the failure to pay tax shown or required to be shown on a return, or if any part of any underpayment is due to negligence or intentional disregard of rules and

regulations or civil fraud. These penalties either are not imposed if the failure is due to reasonable cause, or they require the Service to carry a positive burden of proof. Reasonable reliance on the advice of a tax advisor generally will prevent application of the fraud and negligence penalties.

In 1981, the Congress enacted a "no-fault" penalty on valuation overstatements. Under that penalty, if a taxpayer makes a large error in placing too high a value on property which results in an understatement of tax, then a penalty measured as a percentage of the underpayment resulting from the valuation overstatement is imposed. Although the penalty is imposed without regard to fault, the Secretary may waive all or part of the penalty if there was a reasonable basis for the valuation and it was claimed in good faith.

H.R. 6300

H.R. 6300 would provide for a no-fault interest surcharge that would be nondeductible and payable because of any substantial understatement of tax. A substantial understatement would be one that is at least 10 percent of the taxpayer's actual tax liability and $5,000 or at least 50 percent of the actual tax liability and $500. In these cases, there would be an interest surcharge equal to 20 percent of the interest payable with respect to any underpayment due to the understatement. Thus, the interest surcharge would be 4 percent of the underpayment so due per year, based on the current interest rate of 20 percent. This interest surcharge would be collected as an assessable penalty and applied for the period beginning on the last date prescribed for payment of the tax (without regard to any extensions) and ending on the date of assessment of the tax (or, if earlier, the date of payment of the tax).

The Secretary could waive all or part of the surcharge if the taxpayer showed that there was a reasonable basis for the understatement and that the taxpayer acted in good faith. A waiver would be appropriate, for example, if the taxpayer made a good faith mistake in deciding the proper timing of a deduction. In contrast, a waiver would probably not be appropriate in the case of an understatement arising out of a transaction entered into primarily for tax purposes. In addition, an opinion letter or an appraisal standing alone would not necessarily establish either the reasonable basis for the taxpayer's position or his good faith.

This surcharge would apply to returns due after December 31, 1982. The substantial understatement surcharge would not apply to that portion of an understatement subject to the section 6659 valuation overstatement penalty.

H.R. 5829

H.R. 5829 does not provide for an interest surcharge on substantial understatements; however, it does contain a 10-percent penalty on such understatements. The new penalty for substantial understatement of tax would apply only if the understatement arose out of items not disclosed on the taxpayer's return and would be 10 percent of any underpayment of tax allocable to an undisclosed item from which a substantial understatement arose. An item would be considered disclosed only if information on the return or an attachment to the return is adequate to apprise the Secretary of the nature and amount of the item.

In the case of an individual, an understatement of tax liability would be substantial only if it exceeds the greater of $5,000 or 10 percent of the amount of tax required to be shown on the return; for corporations, the understatement would be substantial only if it exceeds $10,000 or 10 percent of the tax required to be shown on the return.

This penalty would apply to an underpayment in addition to the negligence penalty but would not apply if the fraud penalty or the valuation overstatement penalty is imposed. The Secretary would not be able to waive the penalty.

VI. TAX TREATMENT OF PARTNERSHIP AND SUBCHAPTER S ITEMS

A. Partnership Audits (secs. 601, 602 603, and 604 of H.R. 6300)

Present law

For income tax purposes, partnerships are not taxable entities. Instead, a partnership is a conduit, in which the items of partnership income, deduction, and credit are allocated among the partners for inclusion in their respective income tax returns.

Partnerships are required to file an annual information return setting forth the partnership income, deductions, and credits, names and addresses of the partners, each partner's distributive share of these items, and certain other information required by the regulations.

A penalty is imposed on the partnership for each month (not to exceed 5 months), that a partnership return is late or incomplete. The amount of penalty for each month is $50 multiplied by the total number of partners in the partnership during the partnership's taxable year.

Since a partnership is a conduit rather than a taxable entity, adjustments in tax liability may not be made at the partnership level. Rather, adjustments are made to each partner's income tax return at the time that return is audited. A settlement agreed to by one partner with the Internal Revenue Service is not binding on any other partner or on the Service in dealing with other partners. Similarly, a judicial determination of an issue relating to a partnership item generally is conclusive only as to those partners who are parties to the proceeding.

The Code provides a period of limitations during which the IRS can assess a tax or a taxpayer may file a claim for refund. Generally, the period is 3 years from the date the tax return is filed (if filed before the due date, the due date is treated as the date filed). If more than 25 percent of the gross income is omitted from a return, the statutory period for assessment is 6 years. In the case of a partnership, the income tax return of each of the partners begin that individual partner's period of limitations. Except in the case of federally registered partnerships, the date of filing of the partnership return does not affect the individual partner's period of limitations. In order to extend the period of limitations with respect to partnership items, the IRS is required to obtain a consent for extension of the statute of limitations from each of the partners—not the partnership. Generally, an agreement to extend the period of limitations relates to all items on the return of the partner who consents to the extension.

H.R. 6300

In general

The administration has requested that their partnership audit proposals be included in the H.R. 6300. Under the proposal, the tax treatment of items of partnership income, loss, deductions, and credits would be determined at the partnership level in a unified partnership proceeding rather than in separate proceedings with the partners.

Return filing requirements

Partnerships would continue to file information returns and notify each partner of that partner's share of partnership income, loss, etc. Partners generally would be required to file returns consistent with the partnership return or notify the IRS of the inconsistency. The IRS would be precluded from adjusting consistently reported items without a partnership proceeding. If a partner notifies the IRS of the inconsistent treatment of an item, the IRS may deal separately with that partner, as under existing law, or start a partnership proceeding. Failure to notify would allow the IRS to automatically assess and collect any tax attributable to the inconsistency.

Administrative proceeding

A partnership level administrative proceeding would go through the same process of examination, audit, appeal, settlement, notice of final determination, etc., that generally applies to a tax audit. All partners would be notified by the IRS of the commencement of a partnership administrative proceeding, would be eligible to participate in the proceeding, and would be given notice by the IRS of the final partnership administrative adjustment [FPAA]. Where the partnership return lists more than 100 partners, the IRS would be required to provide notice only to partners with an interest in partnership profits of one percent or greater. A tax matters partner [TMP] would be designated (normally by the general partners, otherwise as prescribed) and would receive notice on behalf of other partners and be required to notify them of the commencement of a proceeding and notice of a FPAA. However, a notice group with an aggregate interest of 5 percent or more in partnership profits may designate a representative in lieu of the TMP to receive notice of a FPAA. The TMP would notify all partners of significant events during the course of an audit, such as conferences, settlement offers, etc.

Settlements

The IRS must, upon settlement with any partner, offer consistent settlement terms to all other partners. The TMP may enter into a binding settlement on behalf of non-notice partners who have not formed a notice group, unless the non-notice partner notifies the IRS that the TMP is not authorized to act on his behalf.

Effect of final partnership administrative adjustment

The FPAA is binding on all partners (unless they are subject to separate proceedings under other portions of the proposal) if a petition for judicial review is not filed within 150 days. The IRS may thereafter, generally within a period of one year, assess any resulting adjustments to the partners' tax liability.

Judicial review of FPAA

Within 90 days after notice of a FPAA, the TMP may file a petition for judicial review. Other partners may not file suit during the 90-day period. Upon expiration of the 90 days, if the TMP does not file a petition, any other partner may file.

Petition may be filed in the Tax Court, the district court for the district in which the partnership has its principal place of business, or the Court of Claims. Only one court acquires jurisdiction and the choice of forum by the TMP always governs. Otherwise, if a petition

is filed in the Tax Court, the Tax Court becomes the forum. Otherwise, the earliest filed petition determines whether the forum is the district court or the Court of Claims. A partner filing in any forum other than the Tax Court must first pay the deficiency resulting from adjustments to his return to reflect the FPAA. Other partners, where the forum is not the Tax Court, would be subject to assessment and collection.

Administrative adjustment requests

The bill provides for an Administrative Adjustment Request (AAR) to be filed within 3 years of the due date for the partnership return. An AAR functions as does a claim for refund. When it is filed by the TMP, it is filed on behalf of all the partners and the IRS may proceed to allow it and grant refunds or institute a partnership proceeding. Failure by the IRS to act within 6 months would enable the partnership to file suit. Petition could be filed in the Tax Court, the Court of Claims, or the appropriate district court and the scope of judicial review would be limited to disallowed items to which the AAR relates. If an AAR is filed by any other partner, unless the IRS commences a partnership audit, it functions as a claim for refund and the IRS may process it as an ordinary claim for refund. If the IRS disallows the request or fails to act, the items to which the request relates are treated as nonpartnership items and the partner may file a refund suit pursuant to section 7422, as under existing law. No suit based on an AAR may be started after the IRS has mailed notice of the commencement of a partnership proceeding (claims made in an AAR would be part of such proceeding).

Statute of limitations

Generally, the period of limitations for assessments attributable to partnership items would be 3 years from the filing of the partnership return, extended by the period during which suit may be filed, by the pendency of court proceedings, and for one year thereafter. The assessment period will not expire with respect to any partner, if the IRS has mailed a timely notice of FPAA, until one year after the IRS is furnished the partner's name and address. For fraud, the period of limitations would be unlimited for partners participating in the fraud and the 3-year period would be 6 years for all other partners. For omissions of 25 percent or more of partnership income, the 3-year period would be extended to 6 years. The limitations period otherwise applicable could be extended by agreement (the TMP would be authorized to enter into an extension agreement on behalf of all partners).

Other matters

(*1*) *Multi-tiered partnerships and pass-through partners.*—Where one partnership (or a trust or subchapter S corporation) holds an interest in another partnership that is the subject of a partnership proceeding, the taxpayer whose liability is affected by the partnership determination is not the immediate partner. If such indirect partners are properly identified and their profits interests disclosed with the partnership return (or thereafter, pursuant to regulation), the IRS will deal with them as the parties in interest for all purposes of the proposals. Otherwise, such indirect partners are bound by any action taken with respect to the pass-through partner.

(2) *Contest of computational adjustments.*—While a partner is precluded from challenging the final administrative or judicial determination of partnership items, he may by claim for refund and by judicial proceeding seek redetermination of the correctness of any computational adjustment to his tax liability resulting from such determination. Substantive issues may not be raised in such proceeding.

(3) *Regulatory authority.*—The proposal authorizes regulations limiting its scope where treatment as partnership items would interfere with effective enforcement of the tax law. This authority would extend to criminal investigations, jeopardy and termination assessments, and other areas presenting special enforcement considerations.

(4) *Foreign-based partnerships.*—The proposal explicitly applies the partnership return filing requirement to any partnership which has U.S. partners (direct or indirect). Where the TMP resides outside the United States or the partnership books and records are kept outside the United States, failure to comply with the partnership return requirement or provide the return information upon request will result in disallowance of partnership losses and credits to the partners. The Secretary would be given authority to waive the reporting requirement in appropriate cases. The bill would also require reporting by a U.S. person who acquires or disposes of an interest in a foreign partnership.

Continuation of existing rules for nonpartnership items

Existing rules relating to administrative and judicial proceedings, statutes of limitations, settlements, etc., would continue to govern the determination of a partner's tax liability attributable to nonpartnership income, loss, deductions, and credits. Neither the IRS nor the taxpayer would be permitted to raise nonpartnership items in the course of a partnership proceeding nor could partnership items, except to the extent the proposal so provides, be raised in proceedings relating to nonpartnership items of a partner. The separate statute of limitations applicable to nonpartnership items of a partner may have expired when the final partnership determination is reached. Neither the IRS (to reduce a refund) nor a partner (to reduce an assessment) may raise nonpartnership items in the computational adjustment of a partner's tax liability attributable to the determination.

H.R. 5829

No provision.

B. Subchapter S Audits (sec. 611 of H.R. 6300)

H.R. 6300 would provide that the determination of items of subchapter S corporations income and loss would be conducted in a unified proceeding with the corporation rather than with each shareholder individually. Generally, the rules applicable to the proposed partnership audit proceedings would apply to subchapter S audit proceedings. However, because subchapter S corporations are limited as to the number and type of shareholders, the proceedings would not need to be subject to all of the partnership rules (e.g. rules applicable to partnerships with more than 100 partners).

VII. MISCELLANEOUS PROVISIONS

A. Paperwork Reduction (sec. 215 of H.R. 6300 and sec. 202 of H.R. 5829)

Present law

Under present law (Paperwork Reduction Act of 1980), information collection requests must be referred to the Office of Management and Budget for approval. The OMB has taken the position that this requirement applies to Treasury Regulations and to tax forms.

H.R. 6300

Under H.R. 6300, the Paperwork Reduction Act of 1980 would not apply to any rule or regulation promulgated under the Internal Revenue Code or to any information collection request that the Secretary determines to be authorized by the Code or by any rule or regulation.

H.R. 5829

The provisions of H.R. 6300 and H.R. 5829 on paperwork reduction are identical.

B. Time for Prescribing Rules and Regulations (sec. 201 of H.R. 5829)

Present law

Present law provides that the Secretary shall prescribe all needful rules and regulations for the enforcement of the Internal Revenue Code, including rules and regulations necessary due to changes in the tax law. There are no specific time requirements for issuance of such rules and regulations.

H.R. 6300

No provision.

H.R. 5829

Under the bill, the Secretary would be instructed to issue rules and regulations pertaining to amendments to the Code made by the bill and any subsequent Code amendments "as soon as possible." Furthermore, the bill would require the Secretary to report annually to the Congress concerning any delays in issuing regulations required by changes in the Code, the reasons for the delay, and progress made in eliminating such delays.

C. Report on Forms (sec. 203 of H.R. 5829)

H.R. 6300

No provision.

H.R. 5829

The bill would require the Secretary, no later than March 31, 1983, to study and report to the Congress methods of modifying the design of the forms used by the Internal Revenue Service to achieve greater accuracy in the reporting of income and the matching of information reports and returns with the actual income tax returns.